EX PARTE OR LATE FILED

AT&T

Suite 1000
1120 20th Street, N.W.
Washington, DC 20036
202 457-3810

July 12, 1996

Mr. William F. Caton
Secretary
Federal Communications Commission
1919 M Street, N.W., Room 222
Washington, D.C. 20554



RE: Ex Parte Presentation
CC Docket 96-98

Dear Mr. Caton:

On Thursday, July 11, 1996, Pam Brander, Steve Garavito and I met with Joseph Farrell per his request. At this meeting we discussed AT&T's previously stated position on the Avoided Cost Model in the Reply Comments of the above-captioned docket. Attached is a summary of AT&T's Avoided Cost Model.

Due to the late hour of the meeting, two copies of this Notice and summary are being submitted to the Secretary of the FCC on the following business day in accordance with Section 1.1206(a)(2) of the Commission's rules.

Sincerely,

Joel Lubin (SW)

Joel Lubin

Attachment

cc: Joseph Farrell

# AT&T AVOIDED COST MODEL

The AT&T Avoided Cost Model (the "Model") is an ILEC and state-specific model that identifies the particular functions that are not applicable to an ILEC's provision of wholesale services and determines an appropriate avoided cost discount. The Model uses publicly available accounting and statistical Automated Report Management Information System ("ARMIS") data, specifically the ARMIS 43-03, 43-04 and 43-08 financial reports for each ILEC, to assign ILEC revenue and expense data to five general ILEC lines of business: Miscellaneous; Private Line; Local; Access; and Toll.

For the Local line of business,[1] the direct retail avoidable costs are identified and removed. These avoided costs are those which are not incurred by the ILEC to provide wholesale service, or are not properly assigned to a wholesale operation. Removal of such avoided costs not only complies with the mandate of Section 252(d)(3) of the 1996 Act, but also helps protect new entrants from being required to subsidize the marketplace efforts of incumbent LECs. The direct costs associated with the following specific USOA accounts are considered avoided:

> Account 5300 - Uncollectibles: These costs are considered 100% avoided because the risk for collection of open accounts receivable moves from the ILEC to the reseller. Further, the risk of non-payment by resellers is negligible when compared to overall uncollectibles.

[1] Local service includes basic area message services such as flat rate local services, measured local services, vertical features and expanded area calling plans.

Account 6610 - Marketing Expense: These costs are specifically identified as avoided in the 1996 Act. Moreover, these costs are not incurred to provide wholesale service and it would be inappropriate for a reseller to subsidize an ILEC's competitive marketing efforts. These costs therefore are 100% avoided.

Account 6620 - Customer Services: These costs are considered 100% avoided because the reseller will assume responsibility for providing customer service to its subscribers.

Account 6220 - Operator Systems Expense: These costs are totally avoided because resellers will either provide their own operators or contract separately with the ILEC or a third party provider for such services.

Account 6533 - Operations Testing, Account 6534 - Operations Plant Administration: These costs are directly associated with customer-facing retail functions that will be assumed by resellers. Based on studies of AT&T customer inquiries and resellers' need to have mechanized interfaces with the ILEC, a minimum of 20% of these costs will be avoided.

The Model next identifies and removes a portion of the indirect retail avoidable costs. A portion of the costs from each of the following USOA accounts is considered avoided and removed based on the treatment of the underlying support asset:

Account 6110 - Network Expense: The portion of network support expense associated with customer-facing retail functions is considered avoided to reflect a reseller's assumption of responsibility for provision of these services.

Accounts 6120 through 6124 - General Support Expense: The portion associated with the provision of retail functions assumed by the reseller is considered avoided.

Account 6560 - Depreciation Expense: The portion associated with assets used in the provision of retail functions is considered avoided.

Account 7240 - Other Taxes: That portion of other taxes that is generated through retail activities to be assumed by the reseller are considered avoided.

Account 7540 - Other Interest Deductions: The portion of these expenses associated with interest on customer deposits is considered avoided.

In addition, the portion of Total Return that reflects the use of support capital in providing retail functions is considered avoided.

A portion of Account 6710, Executive and Planning, and Account 6720, General and Administrative Expense, is also considered avoided. These indirect expenses generally support all services, and, while not attributable to any particular service, they do in fact change as the overall level of services changes. These indirect costs are considered avoided in proportion to the amount of direct costs that are considered avoided. As demonstrated by the regression analysis filed in this proceeding at the Commission's request on June 28, 1996, a statistically significant and proportionate relationship exists between growth in direct costs and growth in indirect costs. Thus, to the extent some proportion of direct costs will be avoided when the ILEC no longer performs a number of retailing functions, a like proportion of indirect retail costs also will be avoided.

Finally, the total avoided retail costs (both direct and indirect) are divided by local service related revenues to derive the avoided retail costs percentage discount, *i.e.*, the wholesale discount.